

**CALIFORNIA STATE BOARD OF EQUALIZATION**  
**APPEALS DIVISION SUMMARY FOR BOARD HEARING**

In the Matter of the Petitions for Redetermination )  
Under the Sales and Use Tax Law of: )  
BLOWFISH, LLC, dba Blowfish, ) Account Number: SR BH 97-015787  
dba Sushi to Die For ) Case ID 484932  
BLOWFISH SR, LLC, dba Blowfish Sushi ) Account Number: SR GH 100-195888  
Case ID 479540  
Petitioners ) City and County of San Francisco

Type of Business: Restaurant  
Audit period: 07/01/04 – 06/30/07 (484932)  
10/01/03 – 12/31/06 (479540)

<u>Item</u>	<u>Disputed Amount</u>	
	<u>484932</u>	<u>479540</u>
Unreported mandatory gratuities	\$186,297	\$165,631
Recorded but not reported sales	\$ 28,119	\$ 14,519
	<u>484932</u>	<u>479540</u>
Tax as determined:	\$19,359.66	\$26,970.65
Adjustment - Appeals Division	<u>00.00</u>	<u>-10,698.93</u>
Proposed redetermination	\$19,359.66	\$16,271.72
Less concurred	<u>- 1,134.26</u>	<u>- 1,409.27</u>
Balance, protested	<u>\$18,225.40</u>	<u>\$14,862.45</u>
Proposed tax redetermination	\$19,359.66	\$16,271.72
Interest through 11/30/11	<u>9,508.30</u>	<u>8,961.62</u>
Total tax and interest	\$28,867.96	\$25,233.34
Payments	<u>- 0.84</u>	<u>0.00</u>
Balance Due	<u>\$28,867.12</u>	<u>\$25,233.34</u>
Monthly interest beginning 12/1/11	<u>\$ 96.79</u>	<u>\$ 81.36</u>

This matter was postponed from previously scheduled hearing dates of April 26, 2011, and May 25, 2011, at petitioners' request so that they could have additional time to file an opening brief. This matter was then rescheduled for Board hearing on July 26, 2011, but was postponed at the request of the Legal Department for further investigation.

**UNRESOLVED ISSUES**

**Issue 1:** Whether the disputed gratuities were mandatory. We conclude that they were mandatory and therefore taxable.

1 Petitioners operated restaurants specializing in sushi. Petitioners' server reports listed two  
2 types of gratuities, "Auto Gratuities" and "Addl. Gratuities," and the audit workpapers contain a copy  
3 of a menu that states "18% gratuity added to parties of six or more." During the audit, petitioner's  
4 controller confirmed that this statement was on petitioner's menus during the entire audit period.  
5 The Department determined that amounts listed as Auto Gratuities were mandatory tips that were  
6 subject to tax. To establish the audited amounts of Auto Gratuities, the Department used a random  
7 selection of server reports to compute the ratio of Auto Gratuities to taxable sales for each business,  
8 and it applied those ratios to audited taxable sales to establish the audited amounts of taxable  
9 mandatory gratuities.

10 Petitioners contend that none of the tips at issue were mandatory. They assert that, since the  
11 controller did not start working for them until near the end of the audit period, she was not  
12 knowledgeable about the menus during the entire audit period, and incorrectly stated that they included  
13 the statement regarding tips. Petitioners also note that Blowfish was previously audited for a period  
14 ending September 30, 2003, and state that a test of guest checks performed during that audit disclosed  
15 no errors.

16 It is undisputed that, at the time of the audit, the Department examined menus including a  
17 statement that an 18-percent gratuity would be added to bills for parties of six or more. On its website,  
18 the to-go menu did not refer to the automatic gratuity or list alcoholic beverages, while the dine-in  
19 menu did. The menu petitioners proffered at the conference did not include the automatic gratuity  
20 statement, but appears similar to the to-go menu on its website and did not list alcoholic beverages.  
21 We conclude the proffered menu is a to-go menu (which petitioner did not disclose when providing the  
22 menu to us).

23 We can think of no logical reason why petitioners would have segregated the tips into separate  
24 categories, including one labeled "Auto Gratuities" except to separately show the gratuities  
25 automatically added to the bill by petitioners and those added by customers. Based on the available  
26 evidence, we conclude that the menus during the audit period contained the automatic gratuity  
27 statement. As for the prior audit, there were no specific comments relating to menus and mandatory  
28 gratuities in the prior audit, and thus the prior audit has no probative value on the issue of the content

1 of the menus during the present audit period. Further, even if petitioners had established that the  
2 menus during the prior audit period did not have the automatic gratuity statement, in the absence of  
3 specific evidence of just when that statement was added, we would have no basis to alter our finding  
4 that the menus contained the automatic gratuity statement during this entire audit period. We conclude  
5 that the gratuities at issue were mandatory and therefore taxable.

6 **Issue 2:** Whether further adjustments are warranted to unreported sales. We recommend no  
7 further adjustments.

8 For most quarters of the audit period, there was a difference between petitioners' recorded sales  
9 tax accrued and their reported sales tax, and for most of these differences, sales tax accrued exceeded  
10 sales tax reported. Except for one quarter for which the sales tax reported exceeded sales tax accrued  
11 by an amount essentially offset by a reverse difference for the prior quarter, the Department accepted  
12 reported sales tax where it exceeded accrued sales tax. For periods where accrued sales tax exceeded  
13 reported sales tax, the Department regarded the difference as unreported taxable sales.

14 Petitioners contended that they reported the correct amount of tax and the tax accrual accounts  
15 do not accurately reflect petitioners' taxable sales. Alternatively, petitioners argue that they should  
16 receive credits for the periods in which sales tax reported exceeds sales tax accrued. Blowfish SR  
17 additionally contends that its entire deficiency should be eliminated because schedules it provided  
18 based on its report of sale system reflect sales that were only \$13,839 more than its reported sales.

19 For Blowfish, we find its sales tax accrual account represents tax reimbursement collected, and  
20 thus evidences taxable sales. We find it improbable that petitioner would have remitted more sales tax  
21 to the Board than it had collected in reimbursement for six of the 12 quarters of the audit period (the  
22 six quarters do not include the one noted above that was offset against an understatement). Petitioner  
23 has the burden to prove that it overpaid tax for those quarters, and it has not done so. Accordingly, we  
24 find no adjustment is warranted to the difference between recorded and reported taxable sales for  
25 Blowfish. For Blowfish SR, we accepted in the D&R that the deficiency should be based on its point  
26 of sale system, which actually disclosed a deficiency of \$14,519. We reject petitioner's argument that  
27 this is close enough to warrant deleting the deficiency altogether. Accordingly, we recommend no  
28 further adjustment.

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26  
27  
28

**OTHER DEVELOPMENTS**

None.

Summary prepared by Thea Etheridge, Business Taxes Specialist II